through stock certificates. It is true that certificates provide the ordinary means of identification. But it is not true that they are the only possible means. Compare Richardson v. Shaw, 209 U. S. 365, 52 L. ed. 835, 28 S. Ct. 512, 19 Am. Bankr. Rep. 717, 14 Ann. Cas. 981; Gorman v. Littlefield, 229 U. S. 19, 57 L. ed. 1047, 33 S. Ct. 690, 30 Am. Bankr. Rep. 266; Duel v. Hollins, 241 U. S. 523, 60 L. ed. 1143, 36 S. Ct. 615, 37 Am. Bankr. Rep. 1. Particularly is this so when, as here, the thing to be established is the allocation of lots sold to lots purchased at different dates and different prices. The required identification is satisfied, if the margin trader has, through his broker, designated the securities to be sold as those purchased on a particular date and at a particular price. It is only when such a designation was not made at the time of the sale, or is not shown, that the 'First-in, first-out' rule is to be applied."

In *Howbert vs. Penrose*, 38 F. (2d) 577 (C. C. A. 10), the Court in its syllabus said:

"2. Where taxpayer claimed that in selling shares of stock in 1918 he sold stock acquired in 1916 and 1917, and sustained loss on sale, proof that certificates delivered by employee of trust company were in most instances those owned by taxpayer before year 1913, rather than those deposited in 1916 and 1917, did not conclusively determine that taxpayer sold stock acquired before 1913."

In the body of the opinion, the Court said:

"In 1918, plaintiff decided to sell the stock acquired in 1916 and 1917, one of the reasons being to enable him to deduct a loss in his 1918 return. He sold the exact number of shares purchased in 1916 and 1917, at an actual loss of $54,030.75. That such was the stock sold is evidenced by the books of his office, and also a pocket memorandum kept by himself. These sales were effected, as were the pur-

chases, through the Colorado Springs office of a broker of the New York Stock Exchange. Delivery by the selling broker was affected by an order on the Columbia Trust Company. An employee of the trust company delivered, in most instances, certificates of the original stock owned by plaintiff, and not the certificates deposited in 1916 and 1917. The government declined to allow the loss incurred, but on the contrary charged plaintiff with a profit of $47,350.50, measured by the difference between the 1918 sale price and the 1913 value of the stock.

"The trial court found as a fact from the evidence, that 'plaintiff intended to and did sell' the shares acquired in 1916 and 1917. The finding is supported by the evidence, and cannot be disturbed. Dooley v. Pease, 180 U. S. 126, 21 S. Ct. 329, 45 L. Ed. 457; Stanley v. Supervisors of Albany County, 121 U. S. 535, 7 S. Ct. 1234, 30 L. Ed. 1000. The trial court likewise found:

"'It has since been ascertained that in the case of many such sales, the certificates so delivered by said depositary were certificates held by plaintiff on March 1, 1913, and in other cases plaintiff is unable to identify the certificates delivered by the depositary on such sales, as those received by it on the purchases above found. In one case only does the proof show that the certificates delivered on a sale were those actually received by the depositary on a purchase above found.'

"The contention of the collector is that the certificates delivered are conclusive as to the identity of the stock sold. Upon this, the trial court, in a memorandum opinion, said:

"'Where a party has held stock for many years, and later buys more, and in this case it is admitted that plaintiff bought a great deal more after 1913 than he sold in 1918, he has a right to decide which stock he is going to sell. The Government has not the

power to say that if the taxpayer sells any of his holdings in a particular company, it can say conclusively that he sold the stock bought at the cheapest price or the shares purchased before or after a certain date. He has the right to decide that himself.'

"In our opinion, proof of the certificates delivered does not conclusively determine what transaction did in fact take place. It is evidence, but not conclusive evidence. So it is of the question of intent of the seller, a point much labored at the trial and here; it is some evidence as to what was done, but not conclusive. The ultimate question is, what was done! It was, and must be readily conceded that if there had been a written contract of the sale of this stock, specifying 'the shares purchased by me in 1916,' and a clerk in the office of a trust company had delivered certificates acquired at an earlier date, the 'identity of the lot' could be and would be determined by the contract. There being no applicable statute of frauds, the finding of the trial court, upon ample evidence, identifies the lot as well as a written contract. * * *"

In *Miller vs. Commissioner of Internal Revenue*, 80 F. (2d) 219 (C. C. A. 2), decided December 9, 1935, we have a decision by the Circuit Court of Appeals which clears out every contention made by the Petitioner herein, and we will quote that decision because it answers every argument which the counsel for the Government made in connection with this matter before the Board of Tax Appeals, and which we believe is an answer to the decision of the Board of Tax Appeals in this case.

The Court in its syllabus said:

"2. Written instructions to broker to sell from taxpayer's safe-keeping account stock bought on specified date at designated price held sufficient identification for income tax purposes, of stock sold pursuant

to that order, though order was fulfilled by delivery of certificates for stock purchased at earlier date.

"3. Certificate of stock delivered by broker should be treated as proper means for identification of stock sold, for income tax purposes, where taxpayer makes no designation of particular stock at time of making sale.

"4. Taxpayer's designation, by instructions to broker concerning shares of stock to be sold, is controlling in identification of stock sold, for income tax purposes, though certificate delivered by broker does not correspond with instructions.

"5. 'First in first out' rule for identification of stock sold for income tax purposes, where taxpayer has purchased different lots of stock at different times applies only where there is no identification of stock sold by certificate delivered by broker or by taxpayer's designation."

The opinion of the Court is as follows:

"AUGUSTUS N. HAND, Circuit Judge.

"This appeal is from a decision of the United States Board of Tax Appeals. It contains a deficiency adjudged to exist in the income tax of the petitioner William W. Miller for the year 1929 arising out of a sale of 500 shares of common stock of Otis Elevator Company, and the dispute is over the proper identification of 300 of these shares, all 500 of which were sold from lots purchased at various times and various prices. The question before us is whether the 300 shares of stock might be identified for income tax purposes by oral and written instructions given by the taxpayer to his broker prior to sale specifying the shares to be sold by dates of purchase and original cost, or whether they could only be identified by the certificate themselves or under the 'First in First out Rule' set forth in section 58, Regulation 78.

"The taxpayer owned 1,735 shares of Otis Elevator common stock on February 25, 1929, which he had purchased at various dates and places. Each certificate was registered in the name of the taxpayer or in the name of Hallgarten & Co., who in general held the certificates for him in a safekeeping account. Whenever the taxpayer's account required additional margin Hallgarten & Co. would withdraw stock from the safekeeping account and place it with other stocks held by the latter as margin and, when no longer required as margin, would return it to the safekeeping account. In some instances this procedure resulted in the merger of certificates representing certain separate blocks. The taxpayer was not advised of these transactions in and out of the safekeeping account.

"On February 25, 1929, the taxpayer directed Hallgarten & Co. in writing to sell 500 shares of Otis Elevator common stock which had theretofore been purchased by them for his account. These shares were designated for sale in written instructions as follows:

100 shares bought March 6, 1926, at 121, $12,125.

100 shares bought March 8, 1926, at 120½, $12,075.

100 shares bought March 9, 1926, at 120¼, $12,050.

100 shares bought December 28, 1926, at 129½, $12,975.

100 shares bought December 28, 1926, at 129½, $12,975.

"There is no question about the identification of the stock bought March 8 and March 9, since the certificates delivered by Hallgarten & Co. were for the shares purchased on those dates. The 100 shares purchased March 6 and the 200 shares purchased

December 28, which were ordered sold, are the items in dispute.

"*The 100 Shares Bought March 6, 1926.*—The order for the sale of this stock was fulfilled by the delivery of certificate No. 6345 from block 6 containing 600 shares, which were registered in the name of Hallgarten & Co. The stock purchased March 6, 1926, had been commingled with the other shares in block 6 so that none of the certificates in the block were traceable to any particular purchase. The Commissioner, and on review the Board of Tax Appeals, applied the 'First in First out Rule' to the transaction, charged the 100 shares sold against the earliest purchases of such stock under article 58 of Regulations 74, instead of charging them against the purchase of March 6, 1926, and computed the profit accordingly for income tax.

"The decision of the Supreme Court in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. ed. 1343, shows that the 'First in First out Rule' should not have been applied to the sale of this lot of stock where the customer had designated the shares to be sold as those purchased on a particular date and at a particular price. To be sure, the court there was dealing with the sale of corporate shares made through a broker which had been held in a marginal account with other lots of the same kind bought at different times and at different prices. But we cannot see why it should make a difference whether a broker has stock belonging to a customer in a safekeeping account or holds it as security for his advances. In each case the title is in the customer and if the broker has advanced money to purchase the stock he holds it only by way of pledge.

"'The designation for sale of the 100 shares bought March 6, 1926, sufficiently identified that stock when sold and the cost of those shares reduced from the original price of $12,125 to the adjusted figure of $8,434.78, by allocation of a part of the cost to other

shares received as stock dividends, was the proper basis for computing any gain which the taxpayer realized from the sale. That figure, rather than $4,612.15 (the adjusted cost of 100 shares purchased March 31, 1934), which the Commissioner used under the 'First-in First-out' rule was the correct basis.

"In Helvering v. Rankin, 295 U. S. 123, 128, 55 S. Ct. 732, 735, 79 L. Ed. 1343, Brandeis, J., said that: 'The required identification is satisfied, if the margin trader has, through his broker, designated the securities to be sold as those purchased on a particular date and at a particular price. It is only when such a designation was not made at the time of the sale, or is not shown, that the "First-in, First-out" rule is to be applied.'

"*The 300 Shares Bought December 28, 1926.*— The order for the sale of this stock was fulfilled by the delivery of certificates Nos. 2694 and 2695 for 200 shares purchased on April 17, 1934, instead of by the delivery of certificates Nos. 3149 and 3152 issued for the stock purchased December 28, 1926, which was ordered sold. The Commissioner argued that these certificates issued for the stock purchased on December 28, 1926, alone represented that stock and neither the designation by the taxpayer of the shares he proposed to sell, nor the 'First-in, First-out' rule could affect the case. But the decisions of the Supreme Court in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343; Gorman v. Littlefield, 229 U. S. 19, 33 S. Ct. 690, 57 L. Ed. 1047; Richardson v. Shaw, 209 U. S. 365, 28 S. Ct. 512, 52 L. Ed. 835, 14 Ann. Cas. 981, and Duel v. Hollins, 241 U. S. 523, 527, 36 S. Ct. 615, 60 L. Ed. 1143, indicate that a designation made at the time of sale sufficiently identifies the stock.

"In Richardson v. Shaw, 209 U. S. 365, 378, 28 S. Ct. 512, 516, 52 L. Ed. 835, 14 Ann. Cas. 981, it was said that: 'A certificate of the same number of shares, although printed upon different paper and

bearing a different number, represents precisely the same kind and value of property as does another certificate for a like number of shares of stock in the same corporation. It is a misconception of the nature of the certificate to say that a return of a different certificate or the right to substitute one certificate for another is a material change in the property right held by the broker for the customer.'

"The certificates of stock involved in Richardson v. Shaw, 209 U. S. 365, 28 S. Ct. 512, 52 L. Ed. 835, 14 Ann. Cas. 981, had been held by a broker on margin and changed many times, and some of them had been released from pledge and delivered to the customer. The broker became bankrupt and his trustee sought to recover the shares which had been delivered to the customer on the ground that the delivery constituted an unlawful preference. The court held that there was no unlawful preference because a certificate of stock was not the property in the shares but only the evidence thereof and a return by the broker of a certificate different from the one purchased was not a material change in the property rights of the customer.

"The Commissioner relies on decisions of the Court of Appeals of the Third Circuit in Horner v. Commissioner of Internal Revenue, 72 F. (2d) 407, Commissioner of Internal Revenue v. Merchants' & Mfgrs.' Fire Ins. Co., 72 F. (2d) 408, and Horner v. Commissioner of Internal Revenue, 78 F. (2d) 813, as showing that the certificate itself governs. But in each of these cases the taxpayer himself had custody of the certificates that he intended to sell, but delivered others to his broker without any special instructions as to the shares to be sold. It was held that intention alone, without designation, could not determine the shares sold. The same result was reached in Skinner v. Eaton, 45 F. (2d) 563 (C. C. A. 2).

Assignment No. II

The Circuit Court of Appeals erred in not holding that where the taxpayer orders certain shares of stock sold, designating such shares by date of purchase, that such designation controls as to the cost of such shares sold as against the cost of certificates delivered by mistake by a bank clerk.

Assignment No. III

The Circuit Court of Appeals erred in not holding that the basis of computing the gain on the stock sold was the cost of shares ordered sold and identified by purchase dates, and not on the basis of the cost of certificates delivered by error by the bank clerk.

Assignment No. IV.

The Circuit Court of Appeals erred in not holding as a matter of law that Petitioner's designation of shares to be sold by the broker sufficiently identified the shares sold, even though the bank clerk, through error, delivered certificates representing other shares to the broker.

Assignment No. V

The Circuit Court of Appeals erred in holding that the delivery of certificates, and the cost thereof, is controlling over a designation by the taxpayer to the broker of specific shares to be sold by dates of purchase, even though the certificates used were delivered by error of a bank clerk contrary to instructions of the Petitioner.

Assignment No. VI

The Circuit Court of Appeals erred in affirming the decision of the Board of Tax Appeals holding that the

cost of the shares sold was determined by the certificates delivered through error by the bank clerk and not the cost of the shares purchased by the Petitioner on March 27, 1929.

Assignment No. VII

The Circuit Court of Appeals erred in holding that the Omaha National Bank was the agent of the Petitioner for the purpose of delivering shares to his broker, and that the Petitioner was bound, for tax purposes, by the mistake of the Omaha National Bank in delivering certificates other than those which the Petitioner ordered the bank to deliver to carry out each of the sales of June 19 and July 1, 1929.

Assignment No. VIII

The Court erred in finding that the one thousand shares of stock in the National Power and Light Co., sold by the Petitioner, in his two sales of June 19 and July 1, 1929, had a cost or other basis for the purpose of detremining gain or loss of $4,420.00 instead of $49,900.00.

Assignment No. IX

The Court erred in finding a deficiency as a matter of law for the year 1929 in the amount of $5,129.20 in lieu of a determination that there was no deficiency in income taxes due from the Petitioner for the year 1929.

ARGUMENT

Facts

As previously stated, the assessment of any deficiency in this matter arises out of the transactions of the Petitioner, James E. Davidson, in National Power and Light Company stock in 1929. All other transactions in stock involved in the appeal to the Board of Tax Appeals were decided by the Board of Tax Appeals as involving no additional deficiency. Therefore, the determination in this appeal involves only the National Power and Light Company transactions of the Petitioner in 1929.

Indeed, we do not have to concern ourselves with any of the transactions except the sale of $1,000 shares of National Power and Light Company stock, the history of which and the Findings of Fact relative to which are shown on page 13 of the Record, and, as previously stated, there is no dispute as to the Findings of Fact. It is the contention of the Petitioner that the law applied to such Findings of Fact creates no deficiency in tax to the Petitioner.

The Petitioner, Mr. James E. Davidson, had held National Power and Light Company stock for several years, and such stock had been put up as collateral to a bank loan and had been held by the bank as collateral since 1925 (Record, page 13). On March 27, 1929, the Petitioner purchased through the broker 1,000 shares of National Power and Light Company stock. The certificates representing this stock were those numbered 80,250 to 80,258, inclusive, and 80,264. It was necessary for the Petitioner to borrow a part of the proceeds from the bank to purchase this stock, and this loan was accomplished with The Omaha National Bank at the time of the purchase of these

1,000 shares. The Petitioner put up as collateral with the Bank the certificates numbered 80,250 to 80,258, inclusive, and 80,264 (Record, page 13). Therefore, up to this step, the identical certificates which represented the shares purchased on March 27, 1929, were held as collateral by The Omaha National Bank for the loan made by the Petitioner to purchase this stock.

There is no dispute under the Findings of Fact that on June 19, 1929, the Petitioner instructed the broker to sell 500 of the 1,000 shares purchased on March 27, 1929, certificates for which were on deposit at The Omaha National Bank. The Petitioner called at the Bank to get the certificates for delivery to the broker, but the Bank refused to release them to the Petitioner, stating that they would make delivery themselves. *It is further undisputed that the Petitioner then instructed the Bank to deliver 500 shares from the certificates numbered 80,250 to 80,258 inclusive, and 80,264, to the broker.* In making delivery of the certificates, however, a bank clerk, *by mistake,* delivered certificates from another lot which had been held as collateral by the Bank since 1925. *The mistake was not known by the Petitioner at that time* (Record, page 14). There is, therefore, no question but that the Petitioner instructed the broker to sell the specific shares purchased on March 27, 1929, which was represented by the certificates which were on deposit at The Omaha National Bank. It is the contention of the Petitioner that this is a specific designation of the shares to be sold.

On July 1, 1929, the Petitioner again instructed the broker to sell the remaining 500 shares purchased on March 27, 1929. When this sale was made, the Petitioner instructed the Bank to deliver to the broker certificates for

500 shares from the remainder of the certificates numbered 80,250 to 80,258, inclusive, and 80,264. Again, however, the Bank made the same mistake and delivered to the broker certificates for 500 shares from the same lot which it had held as collateral since 1925.

The selling price of the first 500 share lot sold by the broker on June 19, 1929, was $28,042.50, and of the second 500 share lot sold July 1, 1929, was $31,392.50. The cost of the 1,000 shares purchased by the Petitioner on March 27, 1929, represented by certificates 80,250 to 80,258, inclusive, and 80,264 was $49,900.00. The cost of the 1,000 shares delivered to the broker by the bank clerk by mistake was $4.42 per share, or $4,420.00 for the 1,000 shares. The deficiency assessed by the Board arises solely out of the profit computed by the Board as the difference between the $4,420.00 and the sale price of the two lots of stock on June 19, 1929, and July 1, 1929, for $59,435.00 (Record, page 14).

The Petitioner contends that under the decisions hereinafter cited he had designated to the broker the specific shares to be sold by amount and by date of purchase and that the shares sold by the broker were the shares which he had ordered the broker to sell. The Bank's error in delivering the wrong certificates did not in any manner affect the order which he had given to the broker to sell. As above stated, there is no dispute that such order was given by the Petitioner to the broker, that such designation was made by the Petitioner to the broker, that the Petitioner tried to get the identical certificates represented by the order to the broker, that the Bank refused to surrender the certificates but made its own delivery, that the Petitioner instructed the Bank to make the delivery of the shares from certificates num-

bered 80,250 to 80,258 and 80,264, and that the Bank clerk, in both instances, made a mistake by delivering other certificates and that this mistake was not known by or made known to the Petitioner.

Law

The United States Supreme Court, and the various Circuit Courts of Appeal, have specifically passed upon the question as to what constitutes a designation of certain stocks or shares when a sale is being ordered thereof and have specifically stated, as a matter of law, that the Petitioner sufficiently identifies the shares to be sold when the Petitioner designates such shares as being those purchased on a particular date.

The Supreme Court of the United States in *Helvering vs. Rankin*, 295 U. S. 123-134, 79 L. Ed. 1343, in its syllabus said:

> "I. As regard the application of the 'first-in, first-out,' regulation of the Treasury Department, relative to computing capital gains and losses for income tax purposes where shares of corporate stock are sold from lots purchased at different dates and at different prices and the identity of the lots cannot be determined, stock carried by a broker on margin for a customer is sufficiently identified by the customer's designating the securities to be sold as those purchased on a particular date at a certain price without identification of the stock certificates, which are carried without being earmarked, in the name of the broker or 'street names,' and have been commingled with like certificates held by the broker for other customers."

In the body of the opinion, the Court said:

> "* * * The fallacy of this argument lies in the assumption that shares of stock can be identified only

In *Millikan vs. Commissioner of Internal Revenue*, 83 F. (2d) 213 (C. C. A. 2), decided April 6, 1936, the facts sufficiently appear in the syllabus and in the opinion of the Court. It will be noted that the margin trader had on deposit with the broker certain shares which were held as collateral by the broker. Subsequent to that time, additional shares were purchased. It was the understanding that the collateral shares were not for sale, except on direction or to protect the account. An order was given to sell 600 shares, without further designation. The Court held that in view of the fact that the collateral shares were not to be sold, the 600 shares ordered sold were sold from the margin account. In the syllabus the Court said:

"1. That broker in confirmation of sale of stock ordered by margin trader had delivered certificates representing certain shares of stock deposited by such trader as collateral held not conclusive as to identity of shares sold for purpose determining profit on sale for tax purposes, where there was undisputed evidence showing that othen shares were actually sold.

"2. Where margin trader had at various times purchased shares of a particular stock and had deposited with broker other shares of same stock as collateral with understanding that collateral shares were not for sale except on direction or to protect account, shares sold when trader merely ordered sale of 600 shares held sufficiently identified for income tax purposes as shares held on margin, in absence of direction to sell collateral or necessity for sale to protect account."

In the body of the opinion the Court said:

"The Commissioner based the deficiency on the theory that the broker delivered certificates representing certain shares of stock deposited as col-

lateral and that this identified the shares sold. But this is not conclusive, for there is undisputed evidence showing that other shares were sold. It was held in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 735, 79 L. Ed. 1343, that, when no certificate is issued to the customer or earmarked or otherwise allocated to him and all certificates for stock are in the name of the broker and are commingled and held by the broker for a common benefit of all dealing in that particular stock, there is no conclusive identification of the shares. The court pointed out that it was a fallacy to assume that the shares of stock can be identified only through stock certificates, saying: 'It is true that certificates provide the ordinary means of identification, but it is not true that they are the only means possible. * * * Particularly is this so when, as here, the thing to be established is the allocation of lots sold to lots purchased at different dates and different prices.'

"It was found by the Board, and it was undisputed, that the collateral stock was accepted by the brokers 'with the definite understanding that said securities are deposited as collateral and not for sale under any circumstances, except as a customer might direct or might be necessary for the protection of the account.' It is conceded that there was no instruction to the brokers to sell any of the collateral stock. Neither was there any sales necessary to protect the account because on that day the margin was ample. It is thus plain that the brokers had no option as to which class of stock was to be sold on petitioner's order. Within Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343, and Miller v. Commissioner, 80 F. (2d) 219 (C. C. A. 2), the petitioner has sufficiently established that the sales here were from the stocks held on margin. * * *"

It will be noted in the foregoing that the Court recognized the designation of stock to be sold because of an agreement or understanding that collateral stocks were

not to be sold and that, therefore, the stock sold was the stock in the margin account. In the case at bar, there was a specific designation of shares of stock to be sold, identified by date of purchase. What better designation could there be by the Petitioner than such a specific lot?

In *Kraus vs. Commissioner of Internal Revenue*, 88 F. (2d) 616 (C. C. A. 2), decided March 8, 1937, the Court in its syllabus said:

"3. In taxation of gain on sale of stock, 'First-in First-out' rule is applicable only, when there is no identification of shares sold with shares purchased, and although stock certificates are not the only means of identification and direction to broker to sell shares designated by date of purchase and price paid will be sufficient to establish identity of stock sold for determining cost basis, notwithstanding that broker actually delivers other certificates than those he was directed to sell, mere intention without more is not designation (Revenue Act, 1928, par. 113 (a) (6), 26 U. S. C. A., par 113, note)."

In the body of the opinion the Court said:

"It may be taken as established that if the petitioner were able to identify the stock he sold with any particular stock he acquired that he would be entitled to take the basis of that stock so identified as the basis of the shares sold. Section 113 (a) (6), Revenue Act of 1928, 26 U. S. C. A., par 113 note. • • • He had the right to sell whatever stock he desired and the right of course to have the taxable gain, if any, computed on the basis of the cost of the particular shares which he elected to sell. • • • A direction to a broker to sell shares designated by date of purchase and price paid will be sufficient to establish identity of the stock sold for determining the cost basis of it even though the broker actually delivers other certificates than those he was directed

to sell, but intention without more is not designation. Miller v. Commissioner, 80 F. (2d) 219 (C. C. A. 2). See, also, Fuller v. Commissioner (C. C. A. 2), 81 F. (2d) 176."

It will be noted that in the foregoing decision, the Court recognizes that the Petitioner has the right to sell whatever stock he desires and that if he so designates the stock he desires to sell, such designation will be controlling, even though other certificates than those he directed to sell are delivered.

Property Right in Shares Sold May Be Identified By Designation of Date Purchased. Certificates Delivered Do Not Represent the Property Itself, But Merely the Evidence of It

In *Richardson v. Shaw*, 209 U. S. 365, 378, 28 S. Ct. 512, 516, 52 L. Ed. 835, 14 Ann. Cas. 981, the question arose whether the delivery of certificates by a broker to a customer amounted to a preference where the certificates delivered were other than those identifying the actual shares purchased by the customer. The Court, in an opinion by Justice Day, said:

"A certificate of the same number of shares, although printed upon different paper and bearing a different number, represents precisely the same kind and value of property as does another certificate for a like number of shares of stock in the same corporation. It is a misconception of the nature of the certificate to say that a return of a different certificate or the right to substitute one certificate for another is a material change in the property right held by the broker for the customer."

In *Gorman v. Littlefield*, 229 U. S. 19, 52 L. Ed. 1047 (1913), Justice Day, in referring to the case of *Richardson v. Shaw*, *supra*, said:

> "In Richardson v. Shaw, 209 U. S. 365, 52 L. Ed. 835, 28 Sup. Ct. Rep. 512, 14 Ann. Cas. 981, the nature of this property was the subject of discussion and decision in this court. In that case a broker, who had been adjudicated a bankrupt, shortly before the bankruptcy, and after his insolvency, turned over upon demand to a customer shares of stock similar to those which had been held for the customer, and for an equal number of shares. It was contended that, under the circumstances, this delivery of certificates amounted to a preference under the bankruptcy act. This court therefore had to consider the legal relation of customer and broker, in buying and holding shares of stock, and it was held that the certificates of stock were not the property itself, but merely the evidence of it, and that a certificate for the same number of shares represented precisely the same kind and value of property as another certificate for a like number of shares in the same corporation; that the return of a different certificate or the substitution of one certificate for another made no material change in the property right of the customer; that such shares were unlike distinct articles of personal property, differing in kind or value, as a horse, wagon, or harness, and that stock has no earmark which distinguishes one share from another, but is like grain of a uniform quality in an elevator, one bushel being of the same kind and value as another. It was therefore concluded that the turning over of the certificates for the shares of stock belonging to the customer, and held by the broker for him, did not amount to a preferential transfer of the bankrupt's property."

Therefore, applying the foregoing law to the present situation, the petitioner ordered the sale of the shares

of stock which he had purchased on March 27, 1929. He had a property right in these shares and it was such property right which he ordered and directed the broker to sell. It was that property right in these shares which he did sell. The certificates were merely evidence of that property right. They did not change that property right and it was still that property right in the shares purchased on March 27, which he sold, even though certificates other than those which represented the purchase of the shares on March 27, 1929, were delivered to consummate the sale.

True Facts, When Found, Take Precedence Over Any Rule

It will be noted in this case that the undisputed fact is that the petitioner ordered the sale of the shares of stock which he purchased on March 27, 1929. No one contends that there was any deceit of the Court on the part of the petitioner in claiming that he ordered the sale of the shares purchased on March 27, 1929. This, therefore, amounts to a finding of the true facts.

In *Rankin v. Commissioner of Internal Revenue*, 84 F. (2d) 551 (C. C. A. 3), the question arose as to the application of the "First-in, First-out" rule. In stressing the consideration to be given to the *true facts*, the Court said:

> "The difference between the taxpayer and the board is that the former reaches the conclusion that the shares directed to be sold were designated and identified as the shares purchased in 1928; the latter views the direction given as merely the declaration of an intention to retain 1,200 shares indifferent as to what shares and without identifying the shares

to be sold. This difference the Supreme Court characterized as 'obviously vital.'

"The view of the board, whether called an expression of opinion or the statement of a conclusion, or, if the expression be preferred, an ultimate fact finding, has in it all the elements of a conclusion of law. Under the evidentiary facts as found, the board concludes that the 'First-in, First-out' rule applies. This is a conclusion of law. The board agrees to the proposition, which is an undisputed one, that if the evidence indicates what shares were sold, the rule does not apply. In reaching the conclusion at which the board arrived, its attention was directed solely to the feature, which it emphasizes, that at the time the sale was directed the shares to be sold were not identified. This overlooks the important, and it seems to us controlling, feature that the designation of what shares were not to be sold was a designation and identification of what were to be sold. The taxpayer owned 2,500 shares. Of these 1,200 had been bought in 1926 with his father's money. These he had directed were not to be sold. There were other shares bought in 1928. When therefore he directed 1,300 shares to be sold, as the 1,200 shares bought in 1926 were not to be sold, his direction was to sell the other stock bought in 1928. It follows that the evidence identifies the stock sold and the rule applied by the board is not applicable."

Therefore, the thing to be determined is the fact, and the fact is undisputed in this case. If the evidence, therefore, discloses what the true fact is, the presumed fact yields to this.

The Circuit Court of Appeals, in its decision (R. p. 37), says:

"While no ulterior purpose is to be attributed to the petitioner in this case, it is not difficult to

perceive that the rule for which he contends may be made the means of tax evasion by collusion between taxpayer and broker."

If, therefore, the Petitioner has established the true t and which is undisputed, why should this Petitioner penalized in being called upon to pay additional in- he taxes just because someone else might use the rule evade taxes if the Government was not sufficiently gent to ascertain what the true fact was?

nk Was Not Agent in Making livery of Certificates

The Circuit Court of Appeals, in its opinion (R. p. , states that the bank in which the certificates were posited as collateral, and the broker who made the sale, re the agents of the taxpayer. The bank was not an nt of the taxpayer in the transaction. The bank had roperty right in any certificates which it held as col- eral. The Petitioner called for the certificates to make livery of them to the broker. The bank refused to let Petitioner take the certificates, saying to the Peti ner that the bank would make its own delivery to pro- t the lien right which they had upon the shares of ck as collateral. This does not change the fact that shares of stock ordered sold were specifically desig- ted as those purchased on March 27, 1929. That was e contract with the broker and it was that contract ich was being carried out. No change was ever made that contract. The certificates were merely evidence the property right and not the property itself. The nk was therefore delivering, not as agent of the Peti- ner, but in the protection of its own lien, the certificates ich they erroneously delivered.

"In Howbert v. Penrose, 38 F. (2d) 577, 68 A. L. R. 820, the Circuit Court of Appeals of the Tenth Circuit decided that book entries and a pocket memorandum kept by the taxpayer furnished sufficient identification, even though no designation of the shares to be sold was communicated to the broker. It is unnecessary for us to express any opinion as to the rule in such circumstances. We only hold that where there is a designation such as was found sufficient in Helvering v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343, it can make no difference whether the stock is held on margin or not.

"This view carries out the purpose of the taxpayer, and we cannot see that it is contrary to sound public policy. If he had ordered a sale of 500 shares of Otis Elevator Stock without instructions as to dates of purchase, and after the sale had stated that he had intended to sell other shares than those evidenced by the certificates delivered, we should not regard his statement as a sufficient designation. But written instructions to sell embodying the number of shares and dates of purchase are an even more persuasive identification of the shares to be sold than the certificates which a broker may deliver without any thought about the particular lot he is selling. The identity of certificates frequently disappears in mergers, consolidations, or split-ups, and a single certificate may be issued in place of various prior ones. A designation by the taxpayer of just the shares he is selling is often the best if not the only available means he has for exercising his option to select the particular shares he desires to sell.

"It follows from the foregoing: (1) That where there is no designation by the taxpayer at the time of making the sale, the certificate should be treated as the proper means for identification; (2) that a designation by instructions to the broker of the shares to be sold is controlling though the certificate delivered does not correspond with the instructions; (3)

that the 'First-in, First-out' rule applies only where there is neither identification by a certificate, nor by designation of the taxpayer.

"The order of the Board of Tax Appeals is reversed, and the proceeding remanded, with direction to determine the amount of tax in accordance with the views we have expressed."

It will be noted here that designation by instructions to the broker of shares to be sold is controlling, though the certificate delivered does not correspond with the instructions. There is no dispute in the Findings of Fact by the Board that the Petitioner ordered the sale of specific stock purchased on a specific date. Therefore, in this case, the Petitioner has complied with the requirement that he designate the specific stock to be sold, and having so designated it, without any question he is entitled to have the basis of any income tax computed upon the difference in cost between the stock ordered and the sale price thereof, without respect to the certificates delivered. The courts so recognize the rule.

In *Fuller vs. Commissioner of Internal Revenue*, 81 F. (2d) 176 (C. C. A. 1), decided January 7, 1936, the Petitioner maintained account books showing the date of purchase of each lot of stock in the Packard Motor Car Company, the number of shares bought, the cost, date and amount of each stock dividend, the date of each sale, the number of shares sold, the sale price and the computation of the profit on each sale. Note that the instructions in this case were given by Petitioner to his assistant to sell those shares which had cost the most and on which the taxable gain would be the least. The Petitioner's assistant examined the ledgers and journals and ascertained therefrom those lots which he claimed were acquired at

the highest prices and instructed the bookkeeper to sell the same. A broker was authorized to make the sales in small lots, and the entire 40,000 shares were sold in April of 1930. Broker sales slips were then recorded on the books. The Circuit Court of Appeals held that such instructions were sufficient to identify the stock sold, and in the syllabus said:

> "Where taxpayer, who maintained account book showing date of purchase of each lot of stock, number of shares bought, cost, date and amount of each stock dividend, date of each sale, number of shares sold, sale price, and computation of profits on each sale, instructed assistant to sell stock which had cost the most, 'first-in, first-out' rule held inapplicable in determining taxable gain, as against contention that stock sold could not be identified because taxpayer had received new certificates in stock split-up (Revenue Act 1928, Paragraphs 22, 111, 112, 113)."

In the body of the opinion the Court said:

> "The Commissioner of Internal Revenue determined that the 25,000 shares thus sold could not be identified and that the provisions of the 'first-in, first-out' rule applied. The Board of Tax Appeals, differing from the Commissioner, adopted the view that the basis for determining the taxable gain derived from the sale of a portion of the stock received in a non-taxable exchange should be determined by apportioning the aggregate costs of all the shares owned by the taxpayer at the time of the exchange to the stock received by him in exchange. It should be said that when the Board of Tax Appeals rendered its decision, Helvering, Commissioner, v. Rankin, 295 U. S. 123, 55 S. Ct. 732, 79 L. Ed. 1343, indicating that certificates do not constitute the only possible means of identifying stock and holding that shares of stock held on margin and sold may be identified by 'desig-

nation' at the time of sale of what lots should be sold and what held, had not been decided. See, also, Miller v. Commissioner, 80 F. (2d) 219, decided December 9, 1935, by the Circuit Court of Appeals for the Second Circuit. As to the view of the Board of Tax Appeals since the announcement of the Rankin decision, see Wieland v. Commissioner, Docket No 73098 (decided October 10, 1935).

"When the taxpayer received certificates of stock in the 1929 'split-up,' so called, his stockholder's interest in the corporation was not changed; it remained precisely what it had been. And the 25,000 shares sold were identified by his directions and by what was done pursuant to them with the specific lots of stock originally purchased in 1925, 1927, and 1928. The cost of such lots constituted the basis for determining the profit on the sale. This taxable gain was included in the taxpayer's return and the tax paid. In our opinion the Commissioner's determination of a deficiency based on the 'first-in, first-out' rule was, under the circumstances, unwarranted. So, too, as to the redetermination of a deficiency by the Board of Tax Appeals.

"The decision of the Board of Tax Appeals is reversed, and the case remanded to that Board, with instructions to reconsider the question before it in accordance with this opinion."

Note that in the foregoing case the designation by the Petitioner was to Petitioner's assistant, who, in turn, instructed the Petitioner's bookkeeper to sell the stocks which cost the most. In the instant case, the undisputed facts show that the Petitioner instructed the broker to sell specific shares which had been purchased at a specific time. There can, therefore, be no question about the sufficiency of designation, and, as stated in the foregoing cases, the fact that other certificates were delivered does not change the order of sale or the shares sold.

Contract With Broker Not Required to Be in Writing

The Circuit Court of Appeals (R. p. 36) said:

> "In the case at bar it is conceded that selling directions were given to the broker. It does not appear from the record that the instructions were written, as they were in the Miller case."

There is no question that there was no applicable statute of frauds requiring that the order given by the Petitioner to the broker had to be in writing. Being in writing would simply be evidence of the fact. In this case the order was made orally. The Court below, as well as the Board of Tax Appeals, found as a true fact that such order was given to the broker. Therefore, the question as to whether it was in writing or was made orally does not enter into the picture. As was said in *Howbert v. Penrose*, 87 F. (2d) 577 (C. C. A. 10), the question as to whether it is in writing or is made orally simply goes to the proof as to what was actually done. The Court said:

> "In our opinion, proof of the certificates delivered does not conclusively determine what transaction did in fact take place. It is evidence, but not conclusive evidence. So it is of the question of intent of the seller, a point much labored at the trial and here; it is some evidence as to what was done, but not conclusive. The ultimate question is, what was done? It was, and must be, readily conceded that if there had been a written contract of the sale of this stock, specifying 'the shares purchased by me in 1916,' and a clerk in the office of a trust company had delivered certificates acquired at an earlier date, the 'identity of the lot' could be and would be determined by the contract. There being no applicable statute of frauds, the finding of the trial court, upon

ample evidence, identifies the lot as well as a written contract. * * *"

Analysis of Decisions Upon Which Circuit Court of Appeals Bases Its Decision

It must be borne in mind that this case does not involve one where there was only an *intention* to sell specific shares without anything more. We have here the uncontroverted fact that the Petitioner went further and designated the specific shares to be sold in his order to the broker.

The decisions upon which the Circuit Court of Appeals relies in the support of its decision deal with cases where there was only an intention to sell specific shares without any designation of the shares to be sold in any order or contract with the broker or third party. This is an altogether different situation than in the case at bar. An analysis of such decision discloses an intention only to sell specific shares without anything more.

In *Horner vs. Commissioner of Internal Revenue*, 72 F. (2) 407, the Petitioner was seeking to base any tax liability upon the cost of stock which he contended *that he intended to sell but which he did not yet own.* In other words, he was trying to convince the Court that the stock which he sold was stock which he did not yet own. There was no designation by instructions of any particular stock to any broker. In the case at bar, we do not have merely an intention to sell, but we do have a specific designation by instructions to the broker of the specific stock to be sold.

In *Commissioner of Internal Revenue vs. Merchants' & Manufacturers' Fire Ins. Co.*, 72 F. (2d) 408, a reading

of the decision discloses that there was no designation of the particular shares to be sold and delivered. In fact, the Court in its opinion says:

> "* * * but the particular shares to be sold and delivered would not be designated." (Page 409.)

In the case at bar we have specific designations by instructions as to the stock to be sold and not only an intention on the part of the taxpayer.

In *Horner vs. Commissioner of Internal Revenue*, 78 F. (2d) 813 (C. C. A. 3), we have again only an intention upon the part of the taxpayer to sell certain stocks, but actually delivering other certificates *without any designation to the broker as to the particular stock to be sold.* Here again is a different situation from the case at bar, where there has been in the case at bar a specific designation by instructions of the stock to be sold.

In *Vawter vs. Commissioner of Internal Revenue*, 83 F. (2d) 11, the Petitioner did not designate to the broker, or to anyone else, the particular stock which he was selling. The Petitioner kept a memorandum on an envelope, which he kept in his possession, of the stocks he intended to sell. It is, therefore, clear from a reading of the decision that if there had been a designation other than a mere intention, the decision of the Court would have been otherwise, because in the opinion the Court says:

> "The burden rested upon petitioner to show that the stock sold in 1930 was that purchased in 1929. Skinner v. Eaton (C. C. A.), 45 F. (2d) 568, certiorari denied, 238 U. S. 837, 51 S. Ct. 486, 75 L. Ed. 1449. It is argued that stock certificates are not the only means by which shares of stock may be identified; that the admitted intention of petitioner to sell

the shares acquired during the preceding year and the memoranda on the envelope were sufficient to discharge the burden. It is settled law that shares of stock can be identified otherwise than through stock certificates, but intention alone is not enough to do so. *There must be a further designation in order to establish the requisite identity.* Helvering v. Rankin, supra, Snyder v. Commissioner, supra; Miller v. Commissioner (C. C. A), 80 F. (2d) 219; Fuller v. Commissioner (C. C. A.), 81 F. (2d) 176; Skinner v. Eaton, supra. The writing on the envelope does tend to corroborate the intention, and it may be conceded that the two combined and considered apart from other facts indicate a sale of the interest in the corporation which was purchased during the previous year; but arrayed in bold contradiction is the fact that, upon receipt of the certificates representing dividends, petitioner removed certificate No. A-5720 from the envelope and placed five of the dividend certificates in it; and, in consummating the sale, he delivered the five certificates to the purchaser and retained the certificate which represented the purchase. * * *" (Emphasis ours.) (Page 13.)

It is therefore clear in the aforecited case that there was no designation of any character as to the stock to be sold, but merely a memorandum upon the taxpayer's own record as to what he intended to sell. This is entirely a different situation than the one in the case at bar, where there was a specific designation to the broker of the stock to be sold.

In *Curtis vs. Commissioner of Internal Revenue,* 89 F. (2d) 736 (C. C. A. 8), the Petitioner had purchased certain stock from the retiring manager. He had made a general agreement with a group of key employees that he would sell to them, not any specified stock, but, an amount of stock which would represent approximately one-third interest in the Company. When the retiring

manager delivered the stock to the Petitioner, the Petitioner took those shares or certificates delivered by the manager and reissued such certificates in his name and these certificates were then deposited with the retiring manager as collateral to secure the balance of the purchase price. Thereafter, the Petitioner issued from other stock which he held the certificates representing the sale to the employees. The petitioner contended before the Court that the certificates of stock or the stock sold to the employees was that purchased from the retiring manager. The answer was, of course, obvious, because the Court said:

> "* * * It falls short of showing that either petitioner or any of the employees had in mind that the stock sold and bought must or should be that represented by the exact certificates held by Schellberg and his wife. No one of the employees so testifies. Petitioner's own actions are proof that the identity of the shares was not material to him since, with complete control of the matter, he deposited these precise shares as collateral and later made the transfer to the employees from other shares." (Page 738.)

There was, therefore, no designation of any particular stock which he would sell to the employees, and there was no contract of the particular stock which they were to purchase. He actually delivered stock from another lot which he had in his possession and had placed the stock which he says he intended to sell as collateral with the purchaser from whom he bought it.

This is an entirely different situation from the facts presented in the case at bar, where there is a specific designation and order for the specific stock to be sold.

In *Cole vs. Helburn*, 4 F. Supp. 20, there was no designation or direction to the broker to sell any specific

stock. If there had been, the decision of the Court would have been different, because the Court says:

> "I cannot sustain plaintiff's contention with reference to the sale of the Atlantic Coast Line Railroad Company stock. He did not direct his broker to sell any particular stock. He simply directed him to sell three hundred shares, and, when the time came for plaintiff to deliver the property sold, he delivered certificates representing the stock purchased by him on February 24, 1928. There is no claim that plaintiff and the purchaser of this stock had any agreement or understanding as to the particular shares of stock involved in the transaction. Therefore, there can be no contention successfully made that the minds of the parties were in agreement, as to the particular shares of stock bought, and that by mistake other and different shares were delivered. The only mistake was made by the plaintiff himself, and for this he must suffer. * * *" (Page 232.)

Here again is a decision where the Petitioner did not designate the specific stock to be sold. There was no agreement or understanding as to the stock to be involved in the transaction. The Court in its decision recognizes that if there had been such a designation of a particular lot of stock, such designation would have been recognized. How different from the situation in the case at bar, where the Petitioner specifically designates the stock to be sold by instructions to the broker and as to which particular lot of stock there can be no question as to identity.

In *Skinner vs. Eaton*, 45 F. (2d) 568, the contention of the taxpayer was based upon statements made by the decedent that he intended to retain his original holdings and that he intended to sell certain stock purchased for return. Again no designation or contract with reference to any specific stock. The Court in its opinion says:

> "In support of their claim, the appellant argue that the sales of 287 shares for 1917 were of stock purchased before March 1, 1913, and 150 shares for 1919 were stock purchased after March 1, 1913, and rely upon the testimony of the associates of the taxpayer, who said that the decedent told them he intended to retain his original holdings in the corporation, and that he intended to sell certain stock purchased for return. These statements are alleged to have been made in 1914 and 1915. The declarations of a taxpayer as to his intention to sell the more recently purchased stock and to retain his original holdings, made orally, are insufficient to change the result. They indicate merely a purpose which he may not have adhered to. They in no way marked the particular shares of stock here under consideration, the identity of which the trial judge has found to have been lost." (Page 570.)

Here again the facts and circumstances were different than in the case at bar. In the cited case, there was merely an expressed intention, while in the case at bar there is a specific and expressed designation by instructions of the stock to be sold.

In *Snyder vs. Commissioner of Internal Revenue*, 295 U. S. 134, we again have a case where there was no designation of the particular stock to be sold, because the Court in its opinion says:

> "* * * The only attempt at identification found by the Board, was the uncontradicted testimony of Snyder to the effect that 'in each case where a sale was made it was his intention to sell the last acquired stock first and shortly thereafter to buy back an equivalent amount in order to increase his margin and acquire additional shares of the stock.' " (Page 137.)

In *Remington Rand vs. Commissioner of Internal Revenue*, 33 F. (2d) 77, the facts and the issue involved

do not in any manner bear any relation to the facts and issue involved in the case at bar. The quotation therefrom that tax liabilities must be determined by what in fact was done does not detract in any manner from the decisions cited by the Petitioner, wherein the Courts have recognized that the designation of a specific stock to be sold to the broker is sufficient evidence of what was done to base any tax liability upon the sale of the stock so designated.

CONCLUSION

We therefore respectfully contend that the proper yardstick in determining the situation is that laid down by Judge Hand in *Miller vs. Commissioner of Internal Revenue,* 80 F. (2d) 219, where at page 221 the Court says:

> "It follows from the foregoing: (1) That where there is no designation by the taxpayer at the time of making the sale the certificate should be treated as the proper means for identification; (2) that a designation by instructions to the broker of the shares to be sold is controlling though the certificate delivered does not correspond with the instructions; (3) that the 'First-in, First-out' rule applies only where there is neither identification by a certificate, nor by designation of the taxpayer."

We respectfully contend that the situation of the Petitioner in the case at bar falls within subdivision (2) of the rule of law above cited in the opinion of Judge Hand. The Petitioner had made a specific and clear designation by instructions to the broker as to the stock the Petitioner ordered sold. Through mistake in delivery, the bank clerk delivered certificates of other stock. Under the rules of law and decisions cited by the respondent,

this did not change the force and effect of the designation which the Petitioner had made to the broker as to the stock which he was selling in that transaction.

We therefore respectfully contend that the Petitioner's contentions should be sustained and that the decision of the Circuit Court of Appeals should be reversed.

Respectfully submitted,

J. A. C. KENNEDY,
YALE C. HOLLAND,
G. L. DELACY,
E. J. SVOBODA,
R. E. SVOBODA,
Attorneys for Petitioner.